

# CHAPTER 1

## **CHAPTER 1**

### **THE BACKDROP**

#### **1.1 PROLOGUE**

The Cooperative Movement in India, born in the first decade of the twentieth century, has, since its inception, focused mainly on the supply of rural finance in general and agricultural finance in particular. The government nurtured the agricultural cooperatives by providing umptin facilities. The entire Movement has been till the present day, dominated by the agricultural cooperatives, and therein by agricultural credit cooperatives. Agricultural cooperatives are catering to the needs of the ruralites pertaining to the production, storage, processing, transport, marketing and credit.

True that the Indian Cooperative Movement was originally ushered in for the supply of rural credit. However, in course of time, the cooperative ideology began to find favour with the urban people, an important manifestation of which is the emergence of non-agricultural credit societies by names like urban cooperative banks, employee's credit societies, etc. to cater to the financial needs of the people of small means such as traders, small producers, artisans, salaried employees, transport operators, small businessmen, and so on. Over the years, this wave of establishing non-agricultural credit societies got a momentum and now they have become a vital part of the urban life of India.

Importantly, unlike the agricultural credit cooperatives in the country, the development of the urban credit societies has been entirely on its own and without any kind of governmental support. For them no targets are fixed, no subsidies are given, no training programmes are organized and no free managerial assistance is provided. Notwithstanding this, the urban credit

societies have increased in numbers, swollen in membership, mobilized plenty of working capital themselves, grown through branch expansion programme, shown considerable efficiency of work and lived for substantially longer period of time embracing a number of decades.

The self-sustained growth of the urban credit societies can well be attributed to the environment in which they functioned. Dense population, educated non-official social workers, considerably bigger turnover, easy availability of cash, conveniently located suitable business premises, easy availability of paid personnel for office work, efforts to update managerial and technological set-ups in order to compete effectively with the commercial banks in the locality. Computerization of their offices ahead even of the commercial bank branches can be viewed as one of the examples. Additionally, they have a personal touch with the clients while doing their business; client-oriented business is their speciality. They do their business without sacrificing profit motive while concomitantly honouring the cooperative principles.

Besides the congenial environment of business, the success of the urban credit societies is very much linked with the enthusiastic, efficient and honest band of persons who were in vanguard and who carried the torch in later years. Leadership of these institutions has provided the moving spirit on the path of their progress and growth. Certainly, this is the key factor in the emergence and satisfactory progress of the urban credit societies. An in-depth study of this factor is conspicuous by absence. This work purports to fill up this void by peeping into the nature and characteristics of the leadership in the Urban Cooperative Banks (UCBs) in Kolhapur city, as it houses such institutions functioning since the second decade of the twentieth century. This broad-based and multi-dimensional investigation will certainly be light bearing.

## **1.2 CONNOTATION OF COOPERATIVE BANKING**

'Banking' is defined by India's Banking Regulation Act, 1949 as accepting for the purpose of lending or investments, of deposits of money from the public, repayable on demand or otherwise and withdraw-able by cheque, draft, order or otherwise, and a 'bank' is one which does the banking business. In this light, a cooperative bank is one which performs the banking functions on a cooperative basis.<sup>1</sup> According to H. Calvert, "Cooperation is a form of organization where persons voluntarily associate together as human beings on the basis of equality for the promotion of the economic interests of themselves."<sup>2</sup> Applying this framework to the banking activity, in the words of Devine; "Cooperative bank is a mutual society formed, composed and governed by working people themselves for encouraging regular saving and granting small loans on easy forms of interest and repayment."<sup>3</sup>

## **1.3 NEED FOR URBAN COOPERATIVE BANKS IN INDIA**

As institutional agencies like commercial banks normally do come forward to help the urban middle class and weaker sections, a strong need to organize urban cooperative banks (UCBs) is felt. There are, in urban areas, numerous persons of small means like traders, merchants, artisans, factory workers, motor and lorry drivers, etc. who need finance. To relieve these persons from the grip of moneylenders, UCBs are essential. The UCBs are basically the institutions of small persons, by small persons and for the small persons. They are local organizations having democratic management and they are serving the persons of small means, ever since the days when the commercial banks were not prepared to look towards them.

Various committees stress the need for UCBs in India from time to time after the birth of the cooperative movement in India in the first decade of the last century.

### **1.3.1 The Maclagan Committee (1915)**

Urban credit societies might serve useful purpose in training the upper and middle classes to understand ordinary banking principles.<sup>4</sup>

### **1.3.2 The Central Banking Enquiry Committee (1931)**

The duty of the urban banks should be to try, to do for the small trader, the small merchant and the middle class population what the commercial banks are doing for the big trader and big merchant.<sup>5</sup>

### **1.3.3 The Cooperative Planning Committee (1946)**

Joint-stock banks are not interested in developing business of small loans, because the cost of advancing and recovering them is high. Further, as joint stock banks are not likely to have under ordinary circumstances full and intimate knowledge of the standing and resources of persons of moderate means, they will not advance on personal security. On the other hand, there are, in urban areas numerous persons of small means like traders, merchants, artisans, factory workers, street hawkers, motor and lorry drivers, who resort to moneylenders and similar agencies for small loans and obtain them at high rates of interests. Cooperative banks qualify, by establishing personal and intimate relationship with people, for this class as the most suitable agencies for serving their credit needs.<sup>6</sup>

### **1.3.4 The Rural Banking Enquiry Committee (1950)**

Urban cooperative banks are useful to cater to the credit needs of people residing at urban, semi-urban and taluka places.<sup>7</sup>

### **1.3.5 The Sub-committee of the Small Scale Industries Board (1956)**

The supply of credit by all existing institutional agencies is not adequate to demand and the proposal for utilization of cooperative urban banks for channeling loans to small-scale industries has to be considered.<sup>8</sup>

### **1.3.6 The Report of the Study Group on Credit Cooperative in the Non-agricultural Sector (1963)**

The urban cooperative banks have an important role to play in several respects including the following:

- (1) First and foremost, they can organize and bring together middle and working classes in urban and semi urban areas.
- (2) The mobilization of savings by urban cooperative banks and the consequent drawing of urban resources into the Apex and Central Cooperative Banks, which are in need of funds to finance the rural, industrial, and other functional cooperatives, can contribute to general economic development.
- (3) By providing credit on reasonable terms to the middle classes, they can rescue them from the exploitation of money-lenders.
- (4) By financing individual industrialists and artisans in urban areas, they can make a significant contribution to industrial development.
- (5) They can provide intelligent, experienced and active leadership to the cooperative movement including the Central and the Apex cooperative Banks, which in view of their federal character draw their directors from member-institutions.<sup>9</sup>

### **1.3.7 The Banking Commission (1972)**

Urban cooperative banks do useful work in mobilizing deposits and

financing the sector of small borrowers. Another useful activity is financing of house construction and repairs for members of the banks. Also this type of banking provides a useful avenue for those who have the necessary ability to set up a bank.<sup>10</sup>

### **1.3.8 The Committee on problems of UCBs in Maharashtra, appointed by Government of Maharashtra (1974)**

The performance of urban banks in Maharashtra, taken as a whole is fairly satisfactory. The sustained growth over the years may be traced to the devoted and selfless management by non-officials. Not only the number of urban banks has increased, but membership, which is a measure of people's involvement, has also increased. Deposits have gone up considerably; the deposits from non-members are more than those of the members, which is a positive proof of the fact that the urban banks have secured the confidence of the depositing public of urban and semi-urban areas.<sup>11</sup>

### **1.3.9 The Madhava Das Committee (1978)**

Despite various limitations, urban banks have mobilized substantial local resources and striven to serve small borrowers. According to the committee, there is scope and need for the development of urban banks in some states. These banks are most suitable for filling up the existing credit inadequacies in urban and semi-urban areas at comparatively lower cost of operation.<sup>12</sup>

### **1.3.10 The Marathe Committee (1992)**

The Committee noted that there is a widespread feeling amongst those connected with the urban cooperative movement that the UCBs will be able to play a much more significant role in the financial system if the present restrictive policies are amended.<sup>13</sup>

### **1.3.11 The Madhava Rao Committee (1999)**

“It is necessary to recognize the strengths and weaknesses of urban cooperative banks in the field of much needed micro credit and how best to foster and encourage UCBs in rendering this service to the small borrower who is not as welcome at the doors of commercial banks, as at the hands of UCBs. The representatives of UCBs and their federations constantly claim that they have a distinct role in the banking sector as they and the small borrowers are made for each other and that any amount of expansion of branch net work of commercial banks, including the RRBs, will not solve the problem of the small borrowers without the presence of UCBs.”<sup>14</sup>

The sum and substance of all these expert committees is as under:

- (1) The urban cooperative banks help to bring together middle and working classes in urban and semi-urban areas. They develop the habits of saving and self-help.
- (2) They collect the resources from urban and semi-urban area and the same are utilized for the development of the area.
- (3) They help to solve the problem of unemployment as small-scale industries and self-employments are labour-intensive. They help to contribute to industrial development.
- (4) Middle classes of the society get finance at reasonable ratio.

## **1.4 LEGAL FOUNDATIONS OF AN URBAN COOPERATIVE BANK IN INDIA**

### **1.4.1 Till 1939**

Initially, most of the urban banks in India were organized as credit societies and later converted into urban banks. Up to about 1939, the term ‘bank’

was loosely used by many societies and there was hardly any distinction between an urban cooperative bank and an urban credit society. While some urban credit societies undertook banking functions without using the word 'bank' or 'banker', there were instances where many urban credit societies not engaged in any banking functions also used the word 'bank' or 'banker'.

#### **1.4.2 The Mehta-Bhansali Committee (1939)**

The Mehta-Bhansali Committee (1939) of Bombay province made an attempt to define an urban cooperative bank. According to this Committee, all urban credit societies having paid up share capital of Rs. 20,000 and over and accepting deposits of money on current account or otherwise subject to withdrawal by cheque, draft or order came within the category of urban cooperative banks. In Madras Province, urban credit societies accepting deposits on current account and maintaining fluid resources according to the standards prescribed by the Registrar of Cooperative Societies were called urban banks. In many provinces, this term was used for credit societies working in urban areas irrespective of the size of share capital or the nature of deposits accepted by them.

#### **1.4.3 The Cooperative Planning Committee (1946)**

According to the Cooperative Planning Committee (1946), urban banks receiving deposits on current account should have (a) a paid-up share capital of at least Rs. 20,000; (b) maintain fluid resources on the scale prescribed by the Registrar of cooperative societies; and (c) carry to the reserve fund at least one-third of their net profits till it equals the paid-up share capital and thereafter at least one-fourth of the net profits. The reserve fund should be invested in gilt-edged securities or deposited in banks approved by the Registrar and should not be used for the business of the bank.

### **1.4.3 The Study Group (1963)**

Recognizing the need for adoption of a uniform definition of an urban bank in the context of the ability of the institution to employ qualified, trained and experienced staff, the Study Group on Credit Cooperatives in the Non-agricultural Sector, appointed by the Government of India under the chairmanship of V.P.Varde in 1963, suggested certain norms. The Group recommended that a cooperative credit society registered under the state cooperative societies act in urban and semi-urban areas having a minimum paid-up share capital of Rs. 50,000 and undertaking the provision of banking facilities could be termed as an urban cooperative bank.

### **1.4.4 Extension of Banking Acts (1966)**

Following the extension of certain provisions of the Reserve Bank of India Act, 1934 and the Banking Regulation Act, 1949 to cooperative banks from 1<sup>st</sup> March 1966, an urban bank is called a 'primary cooperative bank' and defined as a cooperative society, other than a primary agricultural credit society (i) the primary object of which is the transaction of banking business; (ii) the paid-up share capital and reserves of which are not less than Rs. 1 lakh and (iii) the byelaws of which do not permit admission of any other cooperative society as a member. The category of primary cooperative banks also includes salary-earners' societies having paid-up share capital and reserves of Rs.1 lakh or more and the byelaws of which provide for acceptance of deposits from non-members.

In addition to primary cooperative banks, there is a separate category of primary credit societies which are allowed to call themselves as banks, but are kept outside the Reserve Bank's control until their paid-up share capital and reserves come to a level of Rs. 1 lakh or more. The difference between a primary cooperative bank and a primary cooperative credit society is thus only in respect

of their share capital and reserves, the former having paid-up share capital and reserves of Rs. 1 lakh and over and the latter less than Rs. 1 lakh.

In terms of Section 2 (civ) of Reserve Bank of India Act, 1934, a primary credit society has been defined as a cooperative society, other than a primary agricultural credit society, the primary object or principal business of which is the transaction of banking business, the paid-up share capital and reserves of which are less than Rs. 1 lakh, and the byelaws of which do not permit admission of any other cooperative society as a member. Primary credit societies include not only such societies located in urban and semi-urban areas, which accept deposits from the public, but also salary earners' societies having a provision in their byelaws to accept deposits from non-members, the paid-up capital and reserves being less than Rs. 1 lakh in both these categories of societies. Thus the urban cooperative banks (UCBs) differ from the urban cooperative credit societies (UCCSs) in two respects: while some of the provisions of Indian Banking Regulation Act, 1949 are made applicable to UCBs and they are permitted to undertake the subsidiary commercial banking functions, the same is not the case with urban cooperative credit societies.

#### **1.4.5 The Madhav Das Committee (1978)**

Madhav Das Committee Report on UCBs (1978) was the second major landmark development in the urban cooperative banking sector, after the application of Banking Regulation Act, 1949 to UCBs which paved the way for healthy growth of the movement by bringing about the needed financial discipline and control. The Madhav Das Committee suggested that there was a need to stop the practice of primary credit societies commencing banking business without first obtaining license from the Reserve Bank of India. It also recommended that the primary credit societies should not be allowed to sue the

word 'bank', 'banker' and 'banking' as part of their name to enable the public to distinguish between such societies and banking institutions coming under the purview of the Banking Regulation Act, 1949 (AACS). It also listed the corresponding legislative amendments required to give effect to its recommendations. Regarding the existing primary credit societies, the Committee was of the view that such societies might be allowed a maximum period of four years from the date of coming into force of the amended provisions of the Banking Regulation Act, 1949. During the intervening period till such amendments are carried out in the statute, the societies should either reach the level of prescribed viability standards, so as to qualify for the license or take suitable steps to go out of the purview of the Banking Regulation Act, 1949 (AACS).

#### **1.4.6 The Marathe Committee (1992)**

The Marathe Committee (1992) recommended that primary credit societies, which attained the revised entry point norms before 30<sup>th</sup> June, 1993, be considered for inclusion in the list of functioning primary cooperative banks as a one time measure. Such societies should, thereafter, be taken up for inspection and considered for issue of license on the merits. The Committee also suggested that after the expiry of the cut off date of 30<sup>th</sup> June, 1993, the primary credit societies, which do not satisfy the revised entry point norms should discontinue the banking business and the concerned state government should initiate necessary steps in this regard.

#### **1.4.7 Madhav Rao Committee (1999)**

According to new norms, UCBs should have minimum capital of Rs. 4 cr. and membership of at least 3,000 if the population of the place where the urban cooperative bank is being established is more than 10 lakh. For population

between five and ten lakh, the minimum share capital and membership requirements are Rs. 2 cr. & 2,000 respectively. For population between one and five lakh, the corresponding minimum requirements are Rs.1cr. and 1,500 respectively. For towns with population less than 1 lakh, the corresponding minimum requirements are Rs. 25 lakh and 500 respectively.

### **1.5 MEMBERSHIP CRITERIA FOR URBAN COOPERATIVE BANKS**

The membership of an UCB is composed of persons living in urban areas such as traders, merchants, salaried and professional classes, factory workers and labourers etc. Conditions of membership are laid down in the byelaws of each bank. In the banks, there are two categories of members; 'A' class and 'B' class. 'A' class members are the shareholders, who enjoy all benefits of ownership. 'B' class members are 'nominal members'.

The Nominal members are qualified as under:

- (1) Any person who is a co-parcenur or who desires to stand surety for a borrowing member of the bank or who desires to borrow occasionally for a temporary period against certain tangible securities such as gold and silver ornaments and other silver articles, life insurance policies and government and other trustee securities, may be enrolled as a nominal member upon his application in the prescribed form on payment of Rs. 5/- as non-refundable entrance fee and upon his agreeing to the condition that he shall cease to be a nominal member when all liabilities against him either as a borrower or as a surety are fully discharged, provided that such person is one who resides or is gainfully engaged in any occupation within the area of operation of the bank.

- (2) An employee of the bank may be admitted as a nominal member and he will be entitled to the same facilities as admissible to other nominal member.
- (3) A cooperative society registered under the Act shall not be eligible and as such, shall not be admitted to nominal membership in terms of the provisions of the byelaws.
- (4) The nominal members shall not be entitled: (a) to receive share certificate, (b) to receive audited accounts and annual reports, (c) to attend, to participate and to vote in the general meeting and/ or special general meeting of the bank and (d) to receive dividend.

#### **1.6 AREA OF OPERATION OF URBAN COOPERATIVE BANKS**

The existing policy in India regarding area of operation is as under:

- (1) UCBs organized in metropolitan centers or cities may extend their area of operation to the entire limits of the city including the urban agglomeration there of and defined peripheral areas appertaining thereto, UCBs organized in urban/semi-urban centers may extend their area of operation to the entire district of their registration inclusive of rural areas without seeking prior approval of the Reserve Bank of India.
- (2) With prior approval of the Reserve Bank of India, UCBs may extend their area of operation to neighboring district(s) or to the entire state of their registration.
- (3) With prior approval of the Reserve Bank of India, UCBs with deposits of Rs. 50 cr. and above may extend their area of operation even beyond the state of registration.

But banks should send such proposal to the Registrar of Cooperative Societies for prior approval including amendment to their existing bye-laws.

Banks desirous of extending their area of operation beyond the district of their registration as also beyond the state of registration will continue to obtain prior approval of the Reserve Bank of India as hitherto.

### **1.7 MANAGEMENT STRUCTURE OF URBAN COOPERATIVE BANKS**

Like any other cooperative institution, management of an urban bank vests in a board of directors elected by all the members. The tenure of office varies from state to state. The Board of Directors shall consist of 11 directors as under:

- (1) Eleven Directors to be elected from amongst the members of the bank. They should be residing within 10 Km. Radius of the head office.
- (2) In the event of the state government contributing to the share capital of the bank, it shall be entitled to nominate one director on the Board of directors of the bank.
- (3) On the board of directors two seats shall be reserved one for the member belonging to the scheduled castes/ or scheduled tribes and one for the member belonging to the weaker sections. Two seats are reserved for lady members.
- (4) Where the number of permanent salaried employees is 25 or more, the state government nominates one representing such employees. Any person so selected or nominated, as a member of the Board to reserved seat shall not be entitled to be elected as an officer of the bank or to vote at any election of officers.
- (5) In addition to elected and nominated directors, the board of directors may, if so desires, co-opt every year not more than 2 directors from among persons connected with small-scale industries, cottage industries, economists,

financial and banking experts and experienced cooperators. Such directors, however, are not entitled to vote at the meeting of the board and hold the office for one year.

- (6) The chief executive officer shall be the 'ex-officio' member of the board.
- (7) Generally the tenure of the directors is five years.
- (8) The board of directors at its first meeting after the Annual General Meeting elects a chairman and a vice-chairman. Both of them hold office for five years. To give an opportunity to others there may be alteration of chairmanship and vice chairmanship every year as convention.

### **1.8 SOURCES OF FINANCE OF URBAN COOPERATIVE BANKS**

UCBs collect funds for their business from the following sources:

- (1) Shares
- (2) Entrance fees
- (3) Subscriptions
- (4) Deposits
- (5) Interest on loans and advances
- (6) Donations, grants and subsidies.

### **1.9 FUNCTIONS OF URBAN COOPERATIVE BANKS**

- (1) To accept deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft, order or otherwise for the purpose of lending or investment
- (2) To borrow or raise money
- (3) To lend or to advance money either upon or without security to members and others as permitted by the Registrar.

- (4) To draw, make, accept, discount, buy, sell, collect and deal in bills of exchange, hundies, promissory notes, coupons, drafts, bills of lading, railway receipts, warrants, certificates and other instruments and other securities whether transferable or negotiable or not.
- (5) To grant and to issue letters of credit, travelers' cheque and circular notes.
- (6) To buy and sell foreign exchange including foreign bank notes.
- (7) To acquire, hold, issue on commission, underwrite and deal in stocks, funds, shares, debentures, stocks, bonds, obligations, securities and investments of all kinds.
- (8) To purchase and sell bonds, scrips, and other forms of securities on behalf of constituents.
- (9) To receive all kinds of bonds, scrips, valuables on deposit or for safe custody or otherwise.
- (10) To provide safe deposit vaults and ancillary services.
- (11) To collect and transmit money and securities.
- (12) To negotiate loans and advances.
- (13) To carry on and to transact every kind of guarantee and indemnity business on behalf of constituents.
- (14) To effect, insure, guarantee, underwrite, participate in managing and carrying out any issue, public or private or state, municipal or other loans or of shares, stocks, debentures, debenture stock of any company, cooperative society, corporation or association and lend.

- (15) To manage, to sell and to realize any property which may come into the possession of the bank in satisfaction or part satisfaction of any of its claims.
- (16) To open branches and pay offices, with the permission of the Registering Authority and the Reserve Bank of India within the area of operation of the bank so as to provide banking services to the public.
- (17) To acquire, manage and undertake the whole or part of the business of any other cooperative society with the prior permission of the Registering Authority.
- (18) To establish, support or aid in establishment and support of associations, institutions, funds, trusts and conveniences calculated to benefit members, employees/ ex-employees of the bank or the dependents or connections of such persons and grant pensions.
- (19) To provide financial and technical assistance to small-scale and cottage industries and help self-employed persons for setting up their own business.
- (20) To enter into participation, consortium arrangement with any other bank or banks or financial institutions with the object of making loans and advances with the permission of the Reserve Bank of India wherever necessary.
- (21) To do any other form of business as specified in clause (1) of section 6 of the Banking Regulation Act, 1949 (as applicable to cooperative societies).
- (22) To act as agent for collection of monies of government, quasi-government and statutory bodies.
- (23) To grant loans to Cooperative Housing Societies for temporary period pending reimbursement from the Maharashtra Cooperative Housing Finance Society Ltd., Life Insurance Corporation, government and semi-government

**institutions or other financing agencies with the prior permission of the Registering Authority.**

**(24) To undertake any other form of business, which the Central Government may specify as a form of, business in which it is lawful for a cooperative banking institution to engage.**

**(25) To do all such other things as are incidental and conducive to the promotion of advancement of the objects and business of the bank.**

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